IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1940.

No. 551

ANNA L. RAYMOND,
Petitioner,
vs.
COMMISSIONER OF INTERNAL REVENUE.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

REPLY BRIEF FOR PETITIONER.

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I.

Section 22(b)(2) is not applicable to petitioner's annuities.

A. The section does not apply to annuity contracts made with charitable institutions.

Respondent asserts that Senator Harrison, after first indicating that the section does not apply to a taxpayer who purchases an annuity from a charity, thereafter indicated an opposite view in the next few lines of the Con-

gressional Record. (Resp. Br. 6) We challenge that assertion. Plainly the meaning of Senator Harrison's subsequent statements was simply that if an individual should purchase an annuity from an insurance company and upon receiving the annuity payments should turn them over to a hospital, the section would apply to such payments. The Senator in no way modified his prior direct statement regarding annuities purchased from charities. (78 Cong. Rec., Part 6, page 5916.)

Petitioner's contention on this question is also based on the fact that the only grounds on which the section is supported in the Congressional Committee Reports clearly do not apply to annuities purchased from charities. (Pet. 28-29.)

B. Section 22(b)(2) does not apply to annuities purchased before its enactment.

The authorities cited by petitioner (Pet. 12, 30) hold that laws should not operate retroactively unless that intention be clearly declared. There is no declaration of such an intention in Section 22(b)(2).

Respondent relies on cases holding that a revenue act may impose a tax on income received during the year of the act's enactment, and may under certain conditions tax to the settlor the income of a trust created before the law's enactment. (Resp. Br. 7.) Those cases are inapplicable. The income there taxed had been universally recognized as income before the passage of the law; and in

all the cases involving income of trusts, the Court relied on the fact that the income was subject to the settlor's control or was used for his benefit. Therefore the imposition of the tax in those cases could reasonably have been foreseen.

No part of annuity payments received before recovery of their cost had been regarded as income before the enactment of the 1934 Act. It was not reasonably foreseeable when petitioner's annuity agreements were made that a part of the annuity payments would be taxed as income by a subsequent law.

II.

Section 22(b)(2) is unconstitutional.

Neither respondent's brief nor the Congressional Committee Reports quoted therein explain how any portion of annuity payments received before the recovery of their cost "does in fact constitute income." (Resp. Br. 7-8.) The mere assertion to that effect does not change the actual fact nor answer the numerous decisions which indicate the contrary. (Pet. 12-13, 31-34.)

Respondent's attempt to distinguish *Burnet* v. *Logan*, 283 U. S. 404, is unconvincing. (Resp. Br. 8.) That decision was based on the uncertainty of the royalty payments. An equal if not greater uncertainty attends the duration of life of any one individual. Respondent fails to mention any relevant difference in the character of royalty and annuity payments.

The respondent's attempted distinction of the *Logan* case on the ground that it involved no statute corresponding to Section 22(b)(2) wholly begs the question. It was there held that the royalty payments, depending on a contingency, were not subject to income tax, not because of the absence of an appropriate statutory provision, but because they were inherently a return of capital. Consequently any statute which taxed them without apportionment would have violated the Constitution. Neither in that case nor in this can a statute tax capital, without apportionment, as "income."

Respondent's contention that Section 22(b)(2) is analogous to Section 44(a) of the 1934 Act, is without merit. (Resp. Br. 8.) At the time of a sale on the installment plan, the total sale price which the buyer is obligated to pay is definitely known, and is not contingent upon the life of any individual. The vendor is sure to recoup his capital if the buyer's obligations are performed. Therefore the vendor's entire gain can at once be determined and taxed, and the revenue acts prior to 1926 so required. *Nuckolls* v. *United States,* 76 F. (2d) 357, 359 (C. C. A. 10th, 1935). Section 44(a) simply gives the seller *a privilege at his option* of postponing the tax until the receipt of the deferred payments. This privilege may be availed of or waived by any seller. This is clearly pointed out in the cases cited by respondent (Resp. Br. 9). If a seller has elected to postpone the tax, he obviously cannot object if a portion of each installment payment

is treated as income. That is a condition attached to the privilege.

Section 44(a) has not the slightest similarity to Section 22(b)(2), which without any election by the taxpayer taxes, as "income," a portion of annuity payments constituting a return of capital, although the aggregate amount which the taxpayer will recover is wholly contingent and unforeseeable.

III.

The consideration paid for the annuities was the entire amount transferred by petitioner.

If Section 22(b)(2) is inapplicable or invalid, then petitioner's tax liability for 1934 directly depends on the amount of the consideration paid for the annuities. If the entire amount transferred by petitioner was the consideration, as petitioner contends, no part of the annuity payments was income for 1934, and the judgment below was erroneous.

Even if Section 22(b)(2) should be considered applicable and valid, the amount of the consideration paid for the annuities will determine petitioner's tax liability for every year after 1934. Under the Board's view, the entire amount of the first seven annuities, or $57,500.00, will be taxable income in each year during petitioner's life. However, if the entire amount transferred by petitioner was the consideration paid, the consideration will not be recovered tax-free until after 1961, if Section 22(b)(2) be applied; and therefore until at least that year, only so

much of the first seven annuities as equals three per cent of the consideration paid for them, or approximately $34,000.00, will be taxable income in each year. The tax liability of petitioner for the six years from 1935 to 1940 inclusive has already accrued, and its determination will surely require a decision of this question.

A final decision regarding the amount of consideration paid for annuities purchased from charitable institutions will also determine the extent of taxability of all other such annuities, and will enable the Commissioner to treat them all consistently. If the decision below should be allowed to stand, the unfortunate and ill-considered statement of the Circuit Court of Appeals, that the sum which the Board found was the fair cost of the annuities is "more than the actual cost" (R. 152-153), may cause endless confusion. It is important that this question now be settled by this Court, in order to forestall additional litigation regarding the tax liability of petitioner and of all other annuitants of charities.

The respondent's contention that the transfers by petitioner were in part a gift does not answer petitioner's argument on this question. (Pet. 20-26.) An intention of both parties to a contract that one of them shall profit therefrom does not convert part of *the required exchange* into a gift.

The respondent supports the Board's conclusion regarding the amount of the consideration paid only on the grounds that petitioner furnished no other proof on the

question, and that petitioner suggests no other criterion which the Board could or should have adopted. (Resp. Br. 10.)

Petitioner has proved that the criterion used by the Board is arbitrary, erroneous, and contrary to the facts. (Pet. 26-27.) Petitioner's evidence shows that any criterion other than the entire amount transferred can rest only on speculation, conjecture and surmise; and that the only legitimate criterion of the consideration is the entire amount transferred by petitioner. (R. 124-127.)

If a taxpayer proves that the Board's determination of income tax is erroneous and excessive, the Board's decision should be reversed. The burden on the taxpayer is only to prove that the Board's determination is erroneous; not to show the correct tax, or to prove that no tax is due. *Helvering* v. *Taylor*, 293 U. S. 507, 512-516; *Laird* v. *Commissioner*, 85 F. (2d) 598, 601 (C. C. A. 3rd, 1936); *Wilson Coal Land Co.* v. *Commissioner*, 87 F. (2d) 185, 189 (C. C. A. 5th, 1937); *Clements* v. *Commissioner*, 88 F. (2d) 791, 793 (C. C. A. 8th, 1937).

Conclusion.

The decision below is erroneous, irreconcilable with the facts, and in conflict in principle with numerous decisions of this Court and of other Federal Courts. The case involves important questions which should now be settled

by this Court. The petition for a writ of certiorari should therefore be granted.

Respectfully submitted,

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